Market Perspectives
September 2023

KEY HIGHLIGHTS

- September Swoon and the Magnificent Seven
- Fed Signals "Higher for Longer"
- Yields & Oil Up
- Labor Markets, Strikes, and Student Loans
- PCE, Consumer Spending

PERFORMANCE

September lived up to its historical designation as the worst month of the year. The September swoon shaved 4.52% off the S&P 500, 4.62% from the Dow Jones Composite, and 5.13% off the NASDAQ. We wrote last month about seasonal patterns being against us and true to form markets wilted under pressures from higher interest rates, a determined Federal Reserve, and inflationary forces. September also marked the end of the third quarter and the S&P 500 finished down 3.3% making it the first quarterly loss since a year ago. Despite the rough quarter the market has gone up 13.1% since the beginning of the year.

Much ink has been spilt writing about how concentrated stock returns have been. In fact, nearly the entire year-to-date performance of the market cap weighted S&P 500 Index has come from the magnificent seven (AAPL, AMZN, NVDA, MSFT, TSLA, META, GOOGL). Without the performance of these market darlings, stocks would be essentially flat on the year. It doesn't instill confidence in investors when gains are so concentrated.

On the bright side of things, just as history foreshadowed a difficult September, the fourth quarter tends to be the best time of the year for market performance.

Over the last 20 years the fourth quarter has represented three of the four best months for performance and performance has been positive on average nearly 70% of the time.

FED HOLDS THE LINE ON RATES

As has been the case for the last 18 months, markets took queues from the Fed's meeting during September on whether rates would be raised yet again. Taken at face value, the Summary of Economic Projections, also known as the dot plot clearly indicates the Fed thinks one additional hike may be needed. Bond markets aren't so sure as the odds that rates stay on hold for the next four meetings are in the majority and as high as 83% odds, they do nothing at their next meeting Nov. 11th. No one really knows when or if the Fed will move again, but what has been more influential on markets over September has been how long rates stay elevated. Just in September alone, futures markets priced out two rate cuts in

Index	MTD	QTD	YTD	1 Year	2022
S&P 500	-4.77	-3.27	13.07	21.62	-18.11
Dow Jones Industrial Average	-3.42	-2.10	2.73	19.18	-6.86
Russell 2000	-5.89	-5.13	2.54	8.93	-20.44
NASDAQ Composite	-5.77	-3.94	27.11	26.11	-32.61
Europe, Australia, & Far East (EAFE)	-3.37	-4.05	7.59	26.31	-14.05
MSCI Emerging Markets	-2.58	-2.79	2.16	12.17	-19.78
Bloomberg Barclays U.S. Aggregate Bond	-2.54	-3.23	-1.21	0.64	-13.04

Source: YCharts; As of 9.30.23; Returns in percent

2024 and now expect only one rate cut next year. Rates may not be going much higher, but there is now a possibility that they aren't going much lower next year and that has investors nervous.

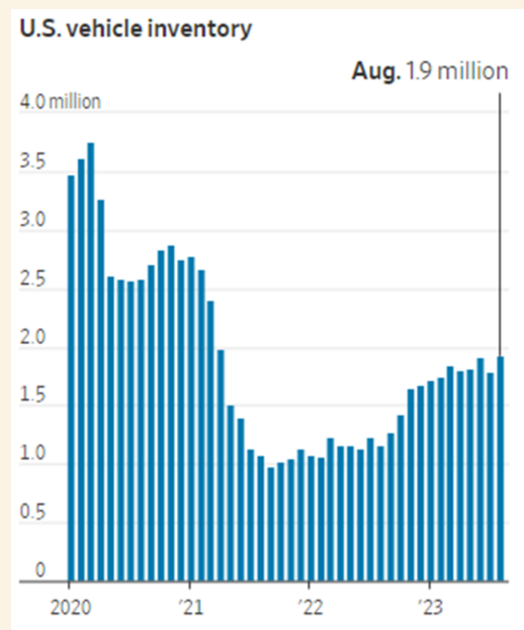
YIELDS & OIL PRICES A TWO-HEADED MONSTER

Outside of the Fed, if you were looking for two other culprits responsible for investors' poor mood in September, look no further than interest rates and oil prices. During September both were notably higher, 10-year yields gained 0.46%, an 11% move higher, and oil gained around $7.5/bbl or 9%. This serves as an economic double-whammy to consumers as they pay more to borrow and more at the pump. Expanding the lens a little further, since April 10-year yields have gone up 1.29% and oil prices are up 48%. Before investors get too carried away, it's good to understand that historically there have only been 10 other times when yields and oil went up simultaneously like this and in only two of 10 occurrences did a recession follow. This dynamic bears watching as consumers continue to feel the pinch and where the U.S. consumer goes, the economy often follows.

STRIKES, LABOR MARKETS, AND OTHER DYSFUNCTION

Labor markets have remained robust over the course of 2023 which has been one of the important pieces underpinning the U.S. economy and one of the main reasons we have been slow to adopt the "hard landing" economic scenario. Economic indicators we follow generally look good and are not red or even flashing yellow. In some cases, the data may be classified as too good and sparking concerns of a hot economy. For instance, September's ISM Manufacturing data came in better than expected and caused interest rates to drift higher. We will learn more about the economy this week as we receive the JOLTS (Job Openings and Labor Turnover Survey) report which provide data on jobs openings, hires, and separations along with the monthly jobs report for September. We're hoping to see continued "goldilocks" results which aren't too strong to move the Fed to raise rates but also not too weak to undercut economic growth.

Some noise in this month's jobs number may be realized as the impacts of the UAW strikes are felt on the numbers while the full economic impact of the strikes won't be known for some time. The big three OEMs warn that by way of parts manufacturers and other ancillary trades there could be as many as 500k workers impacted. Economic impacts of $5B are estimated but in terms of GDP the auto industry represents less than 2.5%. The bigger impact could be on inflation as car supply is just rebounding to healthy levels and therefore prices have eased, down approx. 8% y/y.



Source: Wards Intelligence

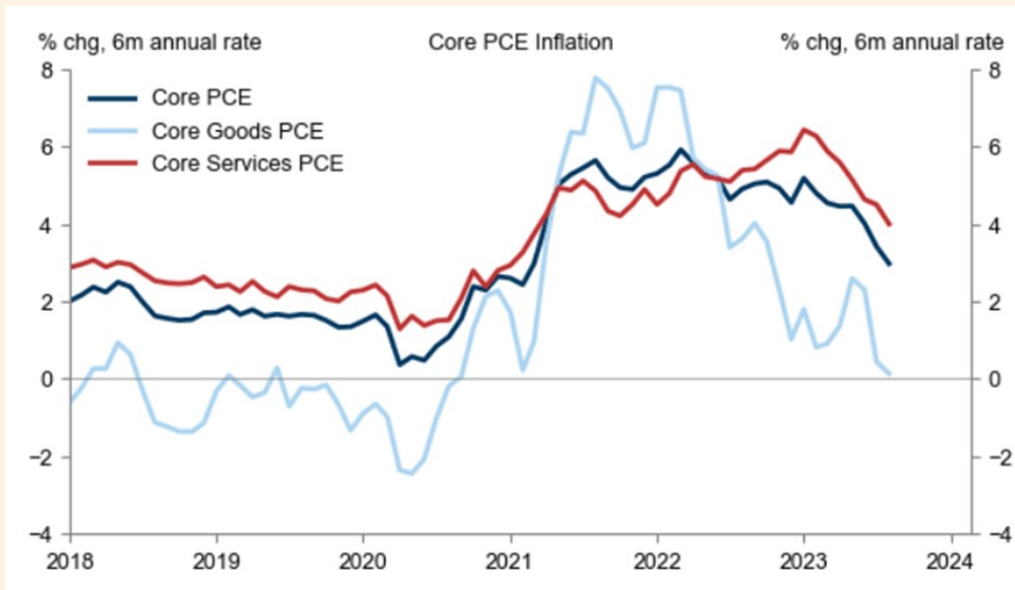
Thankfully we won't be spending much time writing about the government shutdown in our September letter. Congressional leadership was able to get a bipartisan bill passed in a 180 degree about face during the last weekend of September. The stopgap funding measure only gets spending authorized into November so the American public will be exposed to

another round of sausage making beginning late October. Of the $6.4T in budgeted spending for FY 2024, only $1.85T is neither mandatory nor non-interest expense and nearly half of what remains is defense spending. This ultimately leaves very little to haggle about but of this we are certain; the politicians will find a way.

PCE, INFLATION, AND THE CONSUMER

Inflation trends over the month were generally positive as we saw August Core and Headline readings as tracked by CPI meet expectations. The final bit of August data was released last week which showed the Fed's favored inflation gauge, PCE, meet expectations at 3.9% and 3.5% y/y on a core and headline basis, respectively. The last three months through August have annualized at a 2.2% rate. Progress has indeed been made but going forward year-over-year comparisons will become increasingly difficult as much of the inflation surge of 2022 starts to fall out of the trailing 12-mo data set for comparison. Investors should brace for inflation data that moves sideways unless we see a resurgence of outright deflationary data which isn't currently forecast.

Consumers continue to grin and bear the higher cost of life these days. They have largely maintained an anchored view of intermediate to long term inflation which has been a saving grace to the bond market and interest rates. Higher rates have been a burden on consumer pocketbooks, and this is showing up more prevalently in credit card data. Another potential headwind for consumer spending is the resumption of student loan payments which have been on a 42-month hiatus. The good news for now is that consumers are still spending. The bad news is that more and more of it is coming from credit. Goldman Sachs reported last week an increase in credit card losses to 3.63%, up 1.5% from the 2021 trough. They also expect losses to increase to 4.93% and noted the peculiarity of losses increasing outside of an economic recession.



Source: Department of Commerce, Goldman Sachs Global Investment Research

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Sources: YCHARTS, Barron's, NDR, Bespoke, CME Group, FRED